
(1996) 07 KL CK 0065

In the High Court Of Kerala

Case No : Original Petition No. 536 of 1996-S

Commissioner of Income Tax

APPELLANT

Vs

A.V. Thomas and Co. Ltd.

RESPONDENT

Date of Decision : 25-07-1996

Acts Referred:

Income Tax Act, 1961 — Section 256, 35, 35(1)

Citation : (1996) 221 ITR 882

Hon'ble Judges : V.V. Kamat, J;P.A. Mohammed, J

Bench : Division Bench

Advocate : P.K.R. Menon and N.R.K. Nair, for the Appellant; C.N. Ramachandran Nair, for the Respondent

Judgement

V.V. Kamat, J.—The Revenue has brought this petition before us u/s 256(2) of the Income Tax Act, 1961, for a direction to the Income Tax Appellate Tribunal to refer the following five questions on the preparation of the necessary statement of case. The questions are as follows :

"1. Whether, on the facts and in the circumstances of the case, the assessee is entitled to claim deduction u/s 35(1) of the Income Tax Act, 1961 ?

2. Whether, on the facts and in the circumstances of the case, did the assessee-

(i) expend or incur any expenditure on scientific research related to the business ?

(ii) use the entire assets for research ?

(iii) discharge the onus that lay on it for claiming the deduction u/s 35 ?

3. Whether, on the facts and in the circumstances of the case, the Tribunal is right in law and fact in holding that :

(i) the research that is being carried on by the assessee is related to the existing business of the assessee in pesticides and other estate stores" and is not the

above finding wrong, far-fetched and without any reasonable nexus with the existing business ?

4. Whether, on the facts and in the circumstances of the case, does the scientific research in relation to the multiplication of plant that is being carried on have any nexus/relation with the business in pesticides chemical estate, stores, cardamom, pepper when there is "use" of the items dealt in by the assessee in its existing business while multiplied plants are transferred to the fields ? and

(i) is not the above connection/nexus flimsy and untenable ?

(ii) does the above nexus/connection satisfy the relationship contemplated u/s 35 ?

5. Whether, on the facts and in the circumstances of the case, the Tribunal is right in law and fact in holding that the business of the assessee in tissue culture technology oriented plants commenced simultaneously with the research programme ? and

(i) is not the above finding wrong and unreasonable ?

(ii) does the above finding satisfy the tests laid down in Section 35?"

2. Reading the questions, even at the first blush we made it clear to learned senior counsel for the Revenue the obvious factual tint with reference to the contents thereof. We have gone through the three orders only to get the first blush reinforced for confirmation. This is with an additional experience that we find that the first two authorities really did not understand the problem and have approached it in an obviously erroneous manner, how, we will demonstrate hereinafter.

3. The assessment year is 1986-87. With regard thereto the assessee, a company in which public are substantially interested, claimed deduction u/s 35(1) of the Income Tax Act, 1961, for an amount of Rs. 12,08,151. This amount is split up into two categories, viz., Rs. 7,35,164 as revenue expenditure and Rs. 4,72,987 as capital expenditure. The Income Tax Officer has recorded at the outset (see page 9 of the paper book) that the assessee has let in sufficient evidence to show that these items of expenditure relate to the assessee's business of developing plants-tissue-culture technology. The Assessing Officer further observed that there is no material shown by the assessee that the above business was commenced during the year in question. In this connection, reliance was placed on the letter dated January 30, 1989, of the assessee's authorised representative recording that the assessee-company had started a new business of dealing in plants and developing plants as a result of the application of the plants-tissue-culture technology.

4. The assessing authority also refers to the factual aspect showing that the assessee purchased 5,000 plants and these were sold during the year. They are mother plants and still the Assessing Officer has observed that there is no

incurring either of revenue or capital expenditure either with regard to the plant or tissue-culture technology and its use. The confusion becomes obvious when the assessing authority observes that the assessee is not in a position to offer any product manufactured by this technology. It will have to be stated at this stage, as would be crystal clear from the Tribunal's approach that the assessing authority expected the sight of a product as a manufacture in the nature of result of application of the tissue-culture technology. The moment we come to the stage of consideration of the approach of the Tribunal, we would not be detained to realise that the assessing authority did not really see the result of the application of tissue-culture technology- and its essence when it expected the sight of a product as a result of the manufacture by this technology. In this process, the claim was disallowed on the ground that business was not commenced.

5. The next halt of the travel of the proceedings was before the Commissioner of Income Tax (Appeals), Trivandrum. The first appellate authority has also carried forward the same approach to expect a product as a result of the manufacture by application of the technology as the direct aspect expected to be in sight. In paragraph 12 (page 19) of the order of the first appellate authority after reproducing the submissions that the business in tissue-culture technology for propagation of vegetation plants had actually commenced during the previous year ending on December 31, 1984, as would be seen from connected details furnished in the previous assessment year's record for 1985-86. It was submitted that the deduction is claimed in Section 35(1) of the Act on account of research and development activity connected with the business activity, but by application of the plant tissue-culture technology. Reference was also made to the proceedings before the general body meeting, the memorandum and articles of association being required to be amended in connection therewith in support of the contention that the business of dealing in vegetation plants that require application of tissue-culture technology had already commenced as a consequence of the requirement of the amendment in regard thereto. It is also submitted that the use of PTC technology has necessary links with the business of dealing in plants because ultimately the plants are to be sold to outsiders as the assessee did not own any estate for making use thereof. It was also placed for consideration that the assessee had purchased cardamom plants for Rs. 10,971 and sold them for Rs. 11,000. It is also submitted that the research and development expenditure has been already approved by the Department of Scientific and Industrial Research, Ministry of Science and Technology, Government of India, up to December 19, 1984.

6. In spite of these aspects having been placed before the first appellate authority, in paragraph 13 it is observed as follows :

"There is no evidence to show that the assets which were added during the year were utilised for research and development and any product was manufactured using the technology."

7. This would show that the first appellate authority also did not see the realities patent on the face of the record and expected an independent product which is a by-product of the use of the scientific technology.

8. It must be said that the situation required really serious application of mind by the Income Tax Appellate Tribunal, Cochin Bench. The Tribunal also found the situation little heavy for digestion and it must be said to the credit of the presiding members of the Tribunal that they have taken pains in understanding the real situation by going almost to a needed work-place to know the real process.

9. We record our appreciation as we found in paragraph 12 of the order of the Tribunal to the effect that the Bench decided to have a first hand knowledge of the going on in the research stations doing research on plant and tissue-culture and accordingly visited a similar research station at Kakkahad, near Ernakulam, along with the assessee's representative and the Department's representatives. We felt that it is really heartening on the part of the members of the Tribunal.

10. In the process, the Tribunal has observed that the purpose of the research is application and is to produce genetically uniform plants in large numbers in a limited space and time from select mother plants. The process is known as "propagation of plant" propagating through tissue-culture technology widely known as "micro propagation". The Tribunal has also specified the objectives thereof, viz., (a) to vertically increase productivity to be internationally competitive by reducing unit cost, and (b) to achieve excellence in quality and quantity at minimum cost. For development of a rapid multiplication method in 1984 biotech research and development by AVT came to be established. In the sterile areas were located the main shop floor and growth rooms and in non-sterile area is located the media preparation. The application of the tissue-culture technology got concerned with optimal sterilisation technique, media combination and different environmental conditions of storage. After examining the process, the Tribunal has characterised the question relevant for the purpose of consideration of application of statutory provisions of Section 35(1) of the Act, being as to whether the scientific research undertaken and carried out by the assessee known as micro propagation could be considered as related to the business of the assessee or not. The Tribunal has considered that the expenditure of scientific research would be eligible for deduction if the research is "related to the business". In order to find the factual matrix for the answer to the relationship or nexus, the Tribunal has recorded a finding that the assessee is dealing in pesticides, chemicals, other estate stores besides cardamom, pepper, etc. In addition, it renders certain agency services. To be more precise, the Tribunal has recorded that the business of the assessee in relation to the assessment year 1986-87 is in two parts : (a) dealing in certain goods or produces, and (b) rendition of services. The Tribunal has found that the chemicals and other estate stores are necessary inputs for the growth of plant and also to protect the plant from disease and/or decay ; and the research by

the assessee in the plant tissue-culture technology would necessarily lead to the production of genetically uniform plants in large numbers in a limited space and time and when the plants are transferred to the fields, they are to be nurtured by the application of pesticides and other estate stores for the preservation of their lives and protection from disease and decay. As a corollary to this examination of the factual matrix, the Tribunal recorded further that the research being carried on by the assessee is definitely related to the existing business of the assessee in pesticides and other estate store"s.

11. The Tribunal has considered the statutory provisions of Section 35(1). In this connection, it is observed, again factually, that the business of the assessee in tissue-culture technology oriented plants had commenced simultaneously with its research programmes. The Tribunal has supported its above conclusion on the basis of reasons recorded in paragraph 15 of its order. Firstly, it has observed that the research application was processed by the National Chemical Laboratory to record that the transfer of know-how has become complete. Particular reference to item No, 7 of the certificate issued by the N.C.L. would show precisely as to what know-how was given to the licensee. They are procedural details for clonal multiplication of cardamom by PTC technique. The Tribunal has also, in support, referred to the statistics of purchase and sale of vegetation plants to find that in the previous year the assessee had purchased 5,000 mother plants for a sum of Rs. 10,971 ; and this was to record a conclusion that from the mother plants, multiplication would only start by tissue-culture technology application. The Tribunal has observed that the business of the assessee is of growing of genetically uniform plants in large numbers in a limited space and time by applying tissue-culture technology and in this connection it would have to be stated that the business had commenced right from the day when the mother plants were purchased.

12. In the process of reasoning the Tribunal has also fortified its conclusion by reliance on the decision of the Gujarat High Court in Commissioner of Income Tax, Gujrat I Vs. Saurashtra Cement and Chemical Industries Ltd., to spell out what is "commencement of business". In this connection, lastly, the Tribunal observes that it cannot be said that this commencement of business by purchasing of mother plants in the previous assessment years showing the factual situations in regard thereto could not be said not to have been used for the research (sic).

13. We have considered the reasoning of the Tribunal in detail, not only to demonstrate that the situation is a pure question of fact, but also for verification by reinforcement that the Tribunal has really done justice to the situation which is factually in the context. We are also of the view that left to ourselves also we would not have come to any other conclusion that the expenditure, divided as capital expenditure and revenue expenditure, directly displays the necessary and required nexus, when the business of the assessee was of dealing in certain goods or products as well as rendition of service by the use of necessary

scientific technology and connected know-how in regard thereto, commonly known as tissue-culture technology for micro propagation. The questions are purely questions of fact and are not referable at all.

14. For all the above reasons the original petition stands dismissed.